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USDA NATIONAL SERVICE PROGRAM

PROJECT PROPOSAL

I. TITLE: Community Self Development Assistance Corps

II. NARRATIVE DESCRIPTION:

The Department of Agriculture would establish a corps of "professional" and "paraprofessional" members who could assist communities to identify needs and resources necessary for economic well being. This group of individuals would be able to assist communities of all sizes facing economic recovery issues to plan and prioritize efforts items that will work locally. The corps will then assist the community to locate finanancial resources, prepare proposals, design educational programs, and implement strategies necessary to revitalization. The entire focus would be on the community generating their own vision for the future and the USDA corps assisting them in creating and attaining that vision.

III.PURPOSE AND OBJECTIVES:

The purpose of the program would be to provide opportunities for America's youth to "earn and learn." Corps members would be able to earn wages for the work performed, earn a stipend towards further schooling or pay off student loans, and learn valuable skills.
The objectives of the program would be:

- accomplish much needed community planning activities necessary to assure the economic vitality and productivity of our rural and midsized communities
- teach corpsmembers self discipline-skills on coping with the world as adults
- teach specific skills in community building, coalition building, strategic planning and visioning, etc.
- teach numerous skills in working with the "3rd Sector" the private nonprofit sector of the volunteer
- develop skills in working with units of local government which they encounter in their everyday living
- develop community specific cultural leadership skills
- develop skills in career planning and other post-secondary education possibilities

IV. APPROACH:

Most states have local Planning and Development Districts which provide for the overall strategic and project planning efforts for a multijurisdictional area. Some of these cover several counties, and some cover multiple communities within a county or township. They are staffed by local citizens and all have one thing in common. They are understaffed.

This corps would provide trained people with community involvement skills to begin to go into the communities and build from the bottom up the kind of plans that will be able to assure local support for the needed economic changes to occur. The participants would spend a period of training before being assigned to the local districts. They would then live and work in the communities for which they are providing the assistance.

To support these corps members there already exists an information data base at the National Agriculture Library called the National Rural Information Center. This information center maintains a data base of organizations who provide financial support to communites on a national, regional, and local basis. This data base is available to the corpsmembers for assiting the community in developing its own action plan and apply for funding.

V. AUDIENCE AND CLIENTELE:

A major target audience for these programs would be post-secondary education youth. Because of the skill level needed for some of these activities some of the corps members would be already graduated students seeking to pay back their student loans. Others could perform the work either before, after, or during their career development education.

A second target group would be those who are in the process of changing careers. The corps would allow for new career planning and skill building to occur as while the participants continue to support themselves. This would allow the utilization of people already residing in the affected community and would provide a level of realism and continuity to the program.

The communities themselves are also a client. As active participants in the revitalization of their community they will have an increase committment to maintaining the new ecomonic path they have chosen. There will be considerable economic incentives for them to participate.

Finally, as the program expands it could move to include High School youth. This is the age to begin to develop community leadership skills, good work habits, improved self image, and self discipline. This age group could be developed to do the follow-up activities and studies needed to document the success of the efforts. Their could also be a summer program where they are mentored by current community leaders or participate in studies on a short term basis.

VI. POTENTIAL PILOT LOCATIONS:

Thirtytwo states currently have economic development councils or rural development councils so early pilot programs would be easy. Pilot programs could quickly be established in 4 areas of our country:

- o Oregon and Washington
- o Four Courners: Utah, Colorado, New Mexico, and Arizona
- o Tennessee and Kentucky
- o East Texas and Louisiana

These areas already have an existing multiagency coordinating group functioning well and communities that are in dire need of assistance.

VII. ANTICIPATED RESULTS:

There would be multiple outcomes and benefits derived from this program. The outcomes would be local and national at the same time. First there would be the learning while earning of the corps persons themselves. While the objectives of that learning have been chronicled elsewhere it is necessary here to again emphasize its critical importance to our country and to the communities that will come to posses these skilled citizens.

The opportunity to develop skills, to learn about a variety of career paths, and the opportunity to approach career options at a pace not currently available would be other outcomes of the program. With the current economic conditions in our country, it is difficult for youth or people needing to change careers to have the time to do that in a planned and organized way. They feel the pressure to quickly make career choices and begin to earn income. The corps would provide that space to explore options while also providing for food and shelter.

The increased economic viability of our rural communities and small towns is the next major outcome expected. With the assistance of the corps communities will be better able to develop a sound economic base that will take thim into the next century. Results such as increased agricultural production, a viable polution free light industry, increased local tourism, and many other outcomes are possible through planning and implementation of long range stragegies.

Through a mentoring program with current community leaders new leaders would be developed. These practical skills would assist in passing on not only the usual skills, but allow for the passing on of the vital local cultural nuances as well as community spirit. It would allow the older leadership to feel a greater sense of releif to be able to pass on their legacy to a new generation.

VIII. SCHEDULE OF MAJOR TASKS AND COMPLETION DATES:

- July 1, 1993, agencies identify possible pilot project locations and partnerships

- September 1, 1993, have preliminary proposal ready for Corporation for National Service.

- October 15, 1993, complete startup planning for projects submitted

- December 30, 1993, begin final startup phase of projects, begin developemnt of skills training cirriculum, begin development of financial opportunity data base nationally and for pilot states.

- April 1, 1994, begin first training of corps members with assignment to communities at completion of training.

IX. POTENTIAL PARTNERS

- Monday Management Group (17 Federal Agencies involved in rural economic development)
- National Association of Counties
- National Association of Development Organizations
- National Governors Organizatoin
- National Association of Towns and Townships
- National League of Cities
- State Rural Development Councils
- State Economic Development Councils or Agencies

- Local Planning and Development entities both private and public
- National Association of State Foresters
- Department of Defense Agencies such as Corps of Engineers, Air Force. etc/

X. POTENTIAL CAPACITY

At least 100 corps members could be utilized in each state at the peak of the program. During the pilot phase, a cadre of at least 50 would be necessary to provide an adequate network of both professional and paraprofessional skills necessary to reach a significant number of communities.

XI. PROJECT LIAISON

During the start up phase, the project liaison with the Forest Service would be through the Economic Development Staff of Cooperative Forestry. Staff specialist is Steve Yaddoff, 202 205 1386.

During the startup phase, the project liaison with the Rural Development Administration would be through the Norman Ried.

During the startup phase, the project liason with Extension Service would be provided by Randy Williams.

During the startup phase, the project liason with the Soil Conservation Service would be provided by Ed Reichart.

STATUS

May 7, 1993

budgets.upd

1993 STATE RURAL DEVELOPMENT COUNCIL BUDGETS

SRDCs marked with an asterisk will administer their operations budgets through a Federal agency(s). All others will use the Cooperative Agreement between the State and ERS.

1993 BUDGET APPROVED

Alaska
Colorado
Florida
Idaho
Iowa
Kansas
Louisiana
Maine

Missouri
Mississippi*
Montana*
Nebraska
New Mexico
North Carolina
North Dakota
Oklahoma

Oregon*
Pennsylvania
South Carolina*
South Dakota
Texas
Vermont
Washington
West Virginia

subtotal - 24

BUDGET RECEIVED, IN PROCESS

Ohio
Wisconsin

subtotal - 2

Subtotal - 26 SRDCs

MOU SIGNED, BUDGET NOT SUBMITTED

Arkansas
Illinois
Indiana
Kentucky

Maryland
Massachussetts
Michigan
New Hampshire

Utah
Wyoming

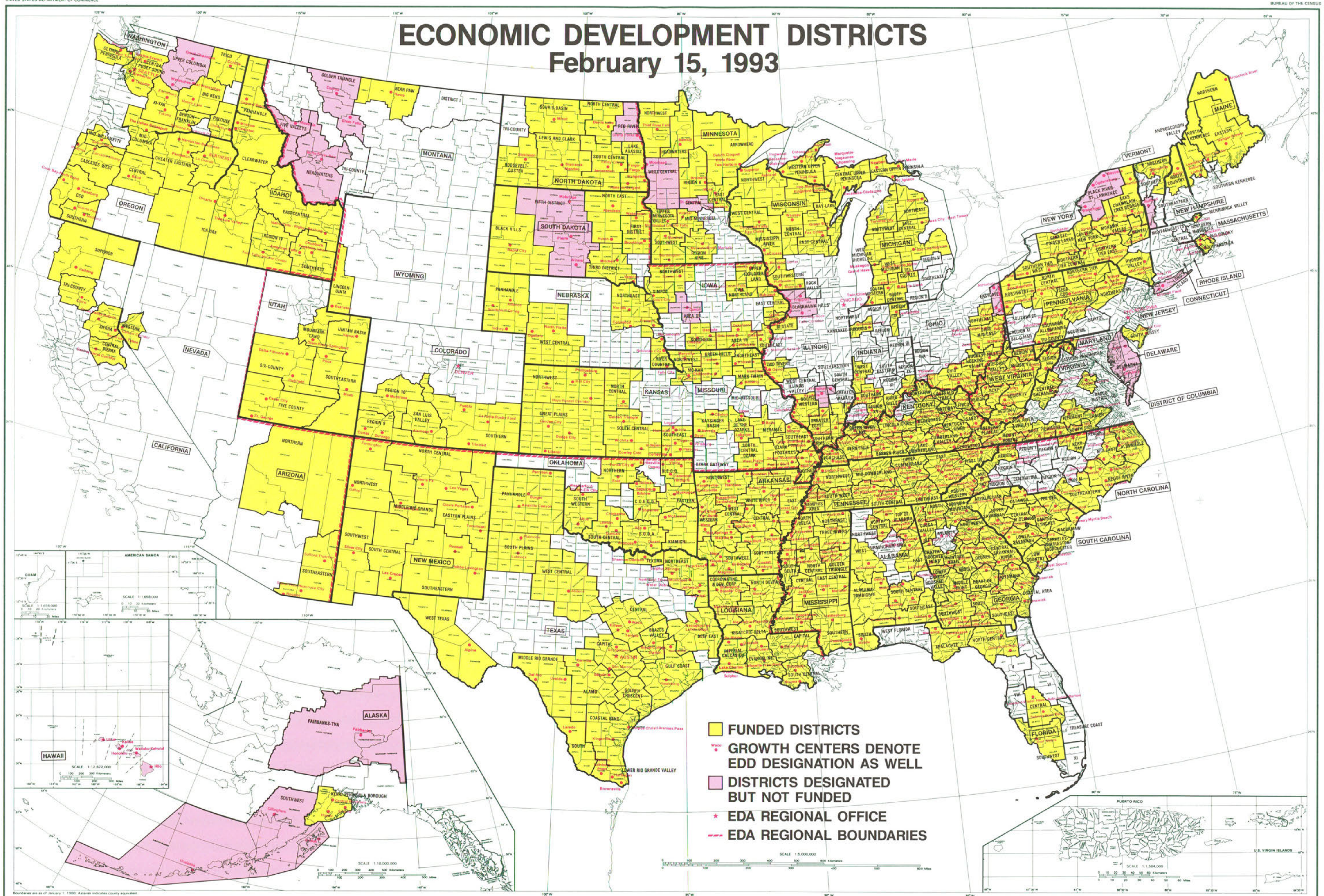
subtotal - 10

Grand Total - 36

UNITED STATES DEPARTMENT OF COMMERCE

BUREAU OF THE CENSUS

ECONOMIC DEVELOPMENT DISTRICTS
February 15, 1993



U.S. DEPARTMENT OF COMMERCE
ECONOMIC DEVELOPMENT ADMINISTRATION

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ECONOMIC DEVELOPMENT DIGEST

Vol. 2, No. 4 | A monthly report for the economic development community | April 1993

Special Rural Development Finance Issue

Clinton's 1994 Budget Proposes Development Banks and Expanded Finance Programs

The President's 1994 budget

President Clinton on April 8 released his first budget, which includes increased funding for several economic development finance programs for fiscal 1994, which begins on October 1. The budget projects $1.52 trillion in spending for FY 1994, representing a 3.2 percent increase over FY 1993 to keep pace with inflation. Domestic discretionary spending accounts for $241 billion, or 16 percent of the budget. This includes spending for all economic development agencies.

The 1,400 page document fleshes out details of the President's economic strategy as outlined in *A Vision of Change for America* which was released February 17 (see March *Digest*). Summarized below are various domestic economic development finance programs as proposed in the President's FY 1994 budget. The amounts listed below do not reflect the amounts requested by the administration in the stimulus package for FY 1993. **Remember: These are the President's recommendations . Actual levels will be decided by Congress in the coming months.**

Community Development Banks

The budget includes $60 million for the US Treasury Financial Management Service for FY 1994 for the creation of a network of community development banks to "provide loans for business and housing purposes in distressed communities that have previously been underserved by traditional

"Clinton" continued on page 2

What are Community Development Banks?

Although there is a great deal of discussion about community development banks, many people are unclear what these institutions are. The four existing community development banks are built upon federally insured and regulated depository institutions that have been organized specifically to promote economic development, or are in simple terms, a bank with a specific mission.

They differ from standard banks by making their primary mission to lend to non traditional borrowers and to stem the capital flow out of distressed areas. The community development banks operating in the United States today are: South Shore Bank in Chicago, Elk Horn Bank and Trust in Arkansas,

"CDB" continued on page 4

In The 1993 Special Issue on Development Finance...

...the *Digest* is focusing on topics that are of particular interest to economic development practitioners working in small business finance. Included are articles on a wide range of topics, from community development banks (above) to microenterprise programs (page 9), as well as a list of organizations that provide information on various development finance programs (pages 10-11). The special center pages focus on revolving loan funds, and federal sources of funding for them.

A publication of the National Association of Development Organizations Research Foundation, NADORF

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Issues for the 1990's: Rural Economy

Rural Enterprise Zones and Economic Development

Richard Reeder (202) 219-0542

Issue. Federal enterprise zones are among the programs proposed to alleviate economic problems in distressed areas. Many States already have enterprise zone programs. But, do they work? How can such a program be designed to help in rural areas?

Context. Distressed areas often suffer from a combination of problems, including poverty, crime, unemployment, and a long history of failed economic development ventures. Many people believe that only a coordinated, multi-dimensional approach can overcome these problems and encourage businesses to grow in distressed areas. Enterprise zones, designated distressed areas that get special government assistance, are advocated as one such approach. In 1992, 35 States had enterprise zone programs. Most States have competitive programs where distressed communities compete with each other in the application process in order to receive State tax incentives for businesses that invest in enterprise zones. In such competitive programs, the State tax incentive lures competing communities to develop strategic plans for revitalizing their economies. These comprehensive plans usually employ a variety of local initiatives, including infrastructure improvements, loans to businesses, streamlined business permit processes, and community crime watch or literacy programs.

Evaluations of State enterprise zones have been generally positive. Some critics had feared that firms would simply relocate from neighboring communities into enterprise zones, but this does not appear to happen very often. Most of the employment growth in zones is due to firm startups or expansion of existing firms. Another fear was that a substantial share of the businesses claiming tax incentives would be free riders; that is, firms that benefit from doing things they would have done anyway. While there is ample evidence of free riding, this has not led to higher program costs per job than in other job creation programs. The most serious problem is that, despite the tax incentives and other zone-associated actions aimed at stimulating the economy, the economic performance of enterprise zones is highly variable, and some zones benefit very little.

Rural zones perform as well as, or perhaps even better than, urban zones, according to evidence from the few studies that examined rural (or small city) enterprise zones. The main drawback for rural areas is that only a small percentage of distressed rural areas have received enterprise zone status. Most large cities have at least one enterprise zone operating within their jurisdiction.

At Stake. Before a new Federal program is enacted, policymakers might want to consider alternative program features that could reduce program costs or increase benefits in rural areas. These include (1) the number of zones, (2) qualifications required for zone designation, (3) duration of zone designation, and (4) assistance provided to the zones. A key consideration in defining these program features is to recognize that when it comes to economic development policy, more is not always better. Emphasis should be on assuring that rural zones will effect productive development strategies.

Alternatives. Any prospective Federal program is likely to be patterned after 1992 proposed legislation, which would have created 25 urban zones and 25 rural zones. Some might argue for more rural zones, because 25 rural zones would cover only a small percentage of distressed rural communities. Expanding the number of zones, however, would add to overall program cost.

Significant expansion of the program could diminish the marketing appeal of the incentive, reducing program effectiveness.

The 1992 legislation would have allowed rural zones to be as large as 10,000 square miles, large enough to encompass several counties in the East, while requiring a population minimum of only 1,000. More restrictive requirements might reduce cost per zone, but the kind of flexibility provided in the 1992 legislation should pay off because it allows clusters of communities and even multicounty areas to work together in creating a coherent regional development strategy.

The 1992 legislation would have entitled each zone to 15 years of tax incentives. While some places might require that long to revitalize their economies, other places might be expected to have a quicker turnaround. If a shorter period, such as 5 years, were employed, program administrators could be given the flexibility to extend zone status for places needing and deserving more time. For places where little effort has been made to implement a development strategy, zone status could be allowed to expire long before the 15-year period is up.

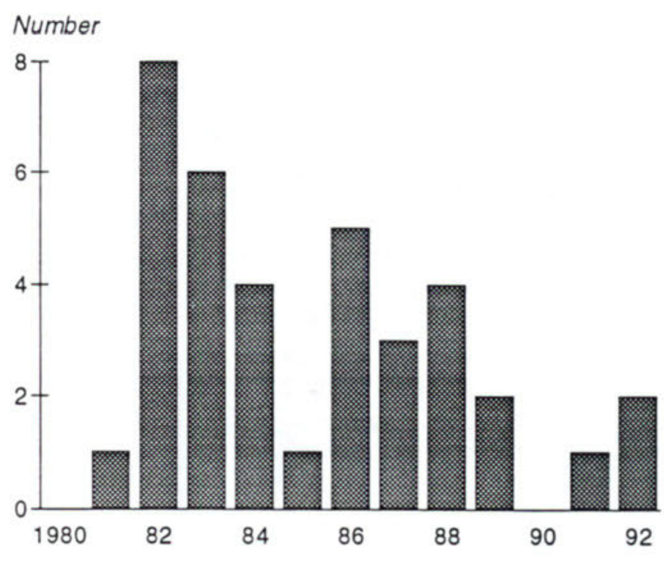
Some have described the 1992 legislation's proposed Federal tax incentives as excessively generous. These incentives include exclusions from capital gains, expensing of stock purchases, wage credits for new hires, losses credited against ordinary income, and additional tax-exempt financing. The estimated cost for just the first 5 years of this program would be $2.5 billion. Policymakers may want to consider only those tax incentives that give the most "bang for the buck," and give zones the opportunity to select among various tax incentives, grants, and loans, so they may fine-tune the package of benefits they receive.

Agenda. Federal legislation is likely in 1993. Some State governments may also consider creating or modifying enterprise zone programs.

Information Sources. Rural performance of State enterprise zone programs: Richard J. Reeder and Kenneth L. Robinson, "Enterprise Zones: Assessing Their Rural Development Potential," *Policy Studies Journal*, Vol. 20. Details on State enterprise zones and Federal enterprise zone proposals, such as the revised version of HR 11 vetoed by President Bush on Nov. 4, 1992: U.S. Dept. of Housing and Urban Development, Office of Community Planning and Development.

Number of new State programs enacted

Interest in State enterprise zones peaked in the early 1980's.



United States
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Issues for the 1990's: *RURAL ECONOMY*

Financial Market Intervention

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Issue. Affordable financing is an important factor in a firm's long-term investment decisions and its day-to-day operations. Adequately financed businesses can adjust to market and technological developments in ways that increase productivity and spur development. Rural financial markets appear to meet the needs of most established rural businesses. But startup businesses, and even mature businesses in some localities, may face financial constraints. The right combination of government-sponsored programs can help alleviate their financing problems, leading to increased investment and rural job growth.

Context. Rural financial institutions and markets have become increasingly integrated with national and international financial markets over the past three decades. But, for the typical small business, financing is still available only from financial service providers having a physical presence in the borrower's community. Since rural communities have few lenders and investors, rural businesses have fewer alternative sources of financing than do their urban counterparts, a particularly vexing problem if local banks and private investors cannot meet a small business firm's financing needs.

Surveys of small businesses indicate that both urban and rural firms are generally satisfied with their access to credit. But research has also shown that entrepreneurs and new firms still in the startup process face severe financing constraints. Regulations imposed to ensure the safety and soundness of the banking system and traditional behavior discourage banks from providing business capital to firms that are not well established. And, a limited supply of investor financing in rural communities means that the vast majority of new businesses must be self-financed. In addition, even well-established creditworthy firms in certain markets may face credit constraints. Small firms located in rural communities served predominantly by large financial institutions may have trouble accessing credit since large banks prefer to make large loans. Conversely, larger firms (but not large enough to directly tap regional financial markets) and firms in a rural community's dominant industry may have trouble finding credit if the area is served by only small lending institutions, which have to be concerned about loan portfolio diversification.

Rural startup businesses having difficulty accessing debt or equity financing are particularly disadvantaged. Formal seed and venture capital funds operate almost exclusively in urban markets where information and transaction costs are minimized. And, rural financial institutions are less likely to take advantage of the risk-sharing financing tools that urban banks use to make risky lending opportunities more attractive. Small rural banks are less likely to originate guaranteed loans, sell loans or loan participations, or refer their customers to other financial service providers. As a result, deals that might be made in a highly competitive urban market are less likely to be made in rural areas.

At Stake. Because of the small size of most rural communities, local financial markets are less competitive than those in urban communities. Investment and job generation in rural America will be slowed if this lack of competition leads to a disparity in access to credit. New business ventures are most likely to be affected, but even well-established firms in certain rural markets may not be able to take full advantage of investment opportunities because of credit constraints. Efforts to foster a vibrant rural economy will be far less successful if the financing needed for worthwhile business opportunities is not forthcoming.

Alternatives. Radical changes in the way credit is allocated are not called for since the existing financial system appears to work well for most businesses seeking debt financing. But, the Federal or State governments can take several steps to improve the operation of rural financial markets. Problems often center around an inadequate exchange of information between borrowers and lenders, and from underuse of alternative sources of funding and mechanisms for distributing risk. Government programs aimed at improving the ability of entrepreneurs and small business owners to prepare realistic business plans and loan applications could reduce loan denials. Other programs that help small banks to evaluate loan requests from new and unfamiliar businesses and to use loan participation arrangements could increase the flow of funds to riskier applicants and to applicants that might wrongly be considered risky. Government support for an information clearinghouse, providing rural bankers with both technical information and easy access to expertise, could help. Easing paperwork and other requirements of loan guarantee programs, such as those operated by the Small Business Administration and the Farmers Home Administration, might also increase their appeal to lenders, making credit more available to riskier loan applicants.

The current system does not always work well for new businesses or rapidly expanding firms needing equity financing in rural areas. Lack of information on alternative sources of financing often discourages rural firms from seeking equity capital. Government support for an information exchange that matches potential investors with prospective entrepreneurs could help. In addition, government-financed seed or venture capital programs specifically aimed at assisting rural businesses could be considered. Most private and public equity funds concentrate their activities in urban areas where fast-growth, high-tech firms are easily found. Public programs aimed at fostering long-term growth in emerging rural industries are rare. Rural areas could benefit if federally assisted small business investment corporations were encouraged to make more equity investments in startup firms rather than making collateral-based loans to existing businesses. Revolving loan funds, which use government appropriations to attract private financing, can also be helpful, particularly if they are chartered to assist new firms. A number of Federal programs provide grants or low-interest loans to help capitalize revolving loan funds, but these funds usually assist expanding businesses rather than startup firms.

Steps encouraging heightened competition within rural financial markets could also benefit rural businesses and residents. Relaxed branching restrictions for banks operating within the State could lead to more competitive rural bank markets in some States. Recent steps to broaden the lending authority of rural electric and telephone cooperatives and the Farm Credit System could eventually increase competition among rural lenders as well. Changes in lending authority need to be carefully considered, however, to ensure that unfair advantages do not ultimately reduce competition in local financial markets. Greater use of Federal and State guaranteed loans and revolving loan programs could further increase interbank competition by encouraging rural lenders to broaden the geographic size of their service areas. As the number of potential lenders increases, rural businesses should find it easier to obtain financing.

Agenda. Proposals have been made to establish a network of privately owned community development banks to lend to new and expanding businesses, and for a small business technical extension service, modelled after the agricultural extension service, to give small businesses easy access to technical expertise. Legislative proposals to allow interstate bank branching and allow the Farm Credit System to begin making loans to rural nonfarm businesses are also expected.

Information Sources. Three U.S. Dept. of Agriculture, Economic Research Service reports: James J. Mikesell and Felice S. Marlor, *Nonmetro, Metro, and U.S. Bank-Operating Statistics, 1990*, SB-846, 1992; Daniel L. Milkove and Patrick J. Sullivan, *Deregulation and the Structure of Rural Financial Markets*, RDRR-75, 1990; and Clifford Rossi, *Rural Conditions and Trends, Special Report on Financial Institutions and Markets*, 1991. Also see: G. Rogers, R. Shaffer, and G. Pulver, "The Adequacy of Capital Markets for Rural Nonfarm Businesses," *The Review of Regional Studies*, Vol. 20, No. 3, Fall 1990.

United States Department of Agriculture

Economic Research Service

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Issues for the 1990's: *RURAL ECONOMY*

Value-Added Agriculture as a Growth Strategy

Dennis M. Brown (202) 219-0525
Mindy F. Petrulis (202) 219-0525

Issue. Many rural areas faced with a declining number of farm jobs consider the food processing sector as a source of potential income and employment growth. By adding value to farm products, the food processing sector is seen by some analysts as a key element of a rural growth strategy.

Context. In 1992, food processing in the United States employed 1.7 million workers in some 20,000 establishments. The sector accounts for 1.3 percent of all jobs and 2.1 percent in nonmetro areas. The food processing sector is small, compared with the farm sector, with 2.5 farm production jobs for every food processing job. The food processing sector, which is quite diverse, comprises 46 food and beverage manufacturing industries, including meatpacking, fruit and vegetable processing, distilling, breadbaking, and ice manufacturing. But, the sector is also highly concentrated, with just seven industries (poultry processing, bakeries, red meat packing, bottled and canned soft drink manufacturing, sausage production, fluid milk production, and miscellaneous food preparations) accounting for more than half of total employment and just under half of all establishments.

Employment in the food processing sector declined 1.7 percent during the 1980's. There is much diversity among food processing industries, in terms of employment changes. Fifteen industries increased employment in the 1980's while 31 experienced losses. Poultry slaughtering and processing gained the most jobs (43,500), followed by miscellaneous prepared foods (16,300). In contrast, the bottled and canned soft drinks industry and red meat packing lost the most jobs (28,500 and 18,800). Sixty-nine percent of all food processing jobs are located in metro counties. Nonmetro food processing jobs are concentrated in just nine industries, which account for two-thirds of all employment.

Nonmetro counties gained nearly 40,000 food processing jobs during the 1980's while metro areas lost 80,000, suggesting some interest on the part of food processors in locating new establishments in nonmetro areas. Nonmetro employment growth in the food processing sector occurred primarily in the poultry slaughtering and processing industry (26,700 jobs) and to some extent in sausage production (7,700), red meat packing (6,800), and the miscellaneous prepared foods industry (6,300). The large-scale growth in the poultry processing industry is due to low-wage labor and a favorable climate in the Broiler Belt (Delmarva Peninsula, the Southeast, Arkansas, and Texas). Nonmetro employment growth in red meat packing during the 1980's was partly caused by a large-scale expansion in the fed cattle industry in the Central and Southern Plains, and an associated decline in processing activity in Corn Belt metro counties.

At Stake. Some rural areas have good prospects for attracting new food processing plants or expanding employment in existing plants. However, reliance on the food processing sector as a critical source of employment growth in the 1990's is likely not a viable option for most local and State economies. No significant employment increases are expected in the sector during the 1990's, partly due to widespread industrial restructuring in food processing during the 1980's. Any gains by rural areas will probably have to come about through intense competition with older, more-established industries in metro areas. Indeed, the process of restructuring, in which many industries underwent mergers and acquisitions and replaced labor with capital investment, has raised questions about the fundamental stability of the sector in certain locations.

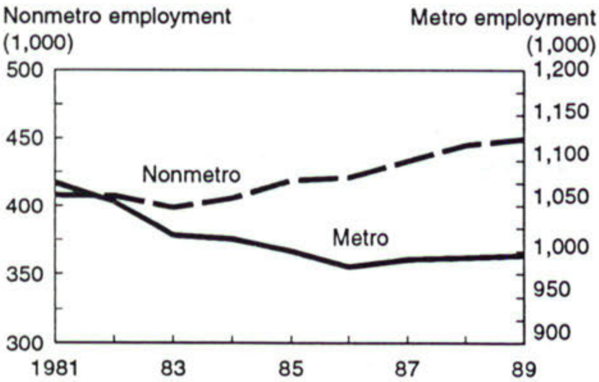
Alternatives. The potential for food processing industries to provide new jobs for a rural community largely depends on whether local areas can supply competitively priced raw inputs for local processing facilities. This means that job prospects in the food processing sector are expected to be confined mostly to areas already specializing in these products. However, new uses of farm products and new crops have received considerable attention as a way to enhance farm income and provide rural jobs. For example, kenaf, an annual hibiscus fiber crop, shows promise in the manufacturing of pulp and paper products such as newsprint or tissue. Guayule, a native shrub of north-central Mexico and southwestern Texas, is a potential source of natural rubber. And, crambe, an annual herb of the mustard family, and rapeseed produce oils that can be further processed into ingredients used in plastics, lubricants, and chocolate substitutes.

Agenda. Most rural areas need to look elsewhere for ways to retain or expand employment. Some may have good prospects based on their natural amenities or proximity to a large city. Others will need to learn how to reduce the costs of rurality—relative isolation, an absence of economies of scale, lack of services—by finding ways to connect rural firms and entrepreneurs to nodes of information, innovation, and finance, and to increase their access to growing global markets. This may require institutional support, such as an industrial extension program, to help firms effectively turn local resources and accessibility into a market advantage.

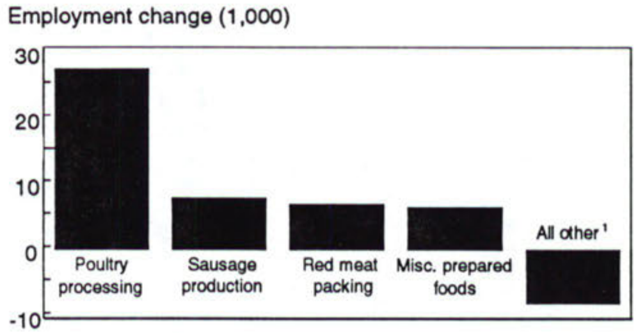
Information Sources. *County Business Patterns*, Bureau of the Census, annual, and *Employment and Earnings*, Bureau of Labor Statistics, monthly.

Metro and nonmetro employment

Employment continued to grow in nonmetro areas and decline in metro areas . . .



...but nonmetro growth is mainly concentrated in four industries.



[1] Represents 23 industries in which employment rose and 19 in which employment declined.

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Issues for the 1990's: Rural Economy

Effect of Bank Consolidation on Rural Credit Availability

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James J. Mikesell (202) 219-0098
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Issue. Bank restructuring affects the local financial markets that rural borrowers rely on for credit and other financial services. While control of rural financial institutions is slowly being transferred to urban-based conglomerates, most banks serving rural areas are still rural headquartered. A reduction in the number of financial institutions serving rural communities might lessen competition and therefore increase the cost of credit or reduce its availability. Proposals to allow interstate banking and branching would accelerate the trend toward fewer but larger banking organizations. Rural business and community leaders worry about how the trend will affect rural economic growth.

Context. The number of commercial banks has declined since the mid-1980's. Part of this reduction is due to bank failures, which initially included many rural-headquartered banks affected by financial problems in the farming and energy sectors. But rural bank failures are now relatively rare. Instead, changes in the size and composition of rural bank markets are due to expansions and mergers of both in-State and out-of-State banking firms. Each State determines the forms of branching and holding company expansion permitted by banking firms already operating in the State, and whether out-of-State bank-holding companies can enter the State by purchasing existing or starting new banks. Most States allow at least some branching by banks chartered within the State, and a large majority permit bank-holding companies based in other States to acquire banks within their jurisdictions. Nonetheless, rural bank offices are not the primary target in most bank acquisitions. And rural banks involved in mergers of bank-holding companies are likely just exchanging one outside owner for another. However, focusing on specific local markets, some mergers do reduce the number of banking firms with a local presence or ownership, and therefore may reduce availability of rural credit. The United States continues to have thousands more banks than other countries, but rural businesses typically have access to just the handful that maintain offices nearby and so can be greatly affected by any change in their local financial markets.

Consolidation of the banking industry can have both negative and positive consequences for rural communities. Some business people and community leaders fear that outside control of rural banks will limit credit availability as local bank deposits are transferred to more profitable outside investment opportunities. Outside banks may also pass up profitable local loans if they fail to accurately evaluate rural loan applications. This may occur because new managers are continually rotated to small rural branches to gain experience before moving on to larger urban offices, or because loan decisions are made by centralized loan committees with limited input from local branches. Those favoring bank consolidation argue that large, geographically diverse banks are less vulnerable to weak economic conditions in a particular region or economic sector. Large banks also provide a wider range of services and products, can handle larger loans, and are less likely to reject loan applications for new types of businesses.

Surveys of small businesses conducted in the 1980's have consistently shown that owners of rural businesses are generally satisfied with their bankers and the availability of bank credit. The data also provide evidence that urban and rural credit markets are well integrated in a national credit market. However, these surveys do not reflect the current regulatory environment that some argue has created a credit crunch. Nor do they provide information on firms that failed or never started due to an inability to obtain credit. Outstanding commercial loans at banks declined during the recession, and the media provided anecdotal evidence of firms that lost access to credit. Nonetheless, it is difficult to determine whether or not credit is harder to find in rural areas compared to urban areas, or compared to conditions that existed in the 1970's and 1980's. Ratios of loans to deposits at rural banks are well below their historical highs. But is this due to a lack of demand as consumers and firms try to reduce debt levels, or does this reflect a widespread refusal by banks to make loans?

At Stake. Banks represent the primary source of credit in most rural communities and therefore directly influence the pace and direction of economic growth. Banks and other lenders were accused of exacerbating the recent recession by being overly conservative in their loan decisions in response to pressure from regulators not to repeat the errors that caused so many financial institutions to fail during the 1980's. Rural consumers and businesses are likely to find themselves operating in financial markets that are becoming more national and global in nature. Rural banking offices will not disappear, but over time more of them will belong to large banking organizations based in distant cities and States. Whether this change has a positive or negative effect on local credit availability depends, in part, on how competitive rural financial markets remain. If local competition is heightened, rural communities stand to benefit from the banking industry's consolidation.

Alternatives. Federal legislation could open the entire country to interstate banking and branching. Variants of this proposal give each State an opportunity to opt out of interstate banking by passing appropriate legislation within a specified timeframe, or require States to pass enabling legislation to participate in interstate banking. Large bank-holding companies argue that they could operate more efficiently, with benefits passed on to all of their customers, if they were able to convert bank affiliates to bank branches and to enter any market rather than those dictated by individual States.

Experience in States that have permitted widespread branching for many years suggests competition within local markets need not suffer when large urban-based banks move into rural markets. A significant proportion of community banks endure and prosper in statewide branching environments by identifying and serving markets and customers ignored by large banking organizations. This is likely to be the case whether or not interstate banking legislation is passed, as long as the current Federal Deposit Insurance System remains unchanged.

Some proposals for changing the current bank deposit insurance system could penalize rural banks. The system was designed to protect both individual depositors and the broader financial system by assuring that failure of one bank does not scare people into removing deposits from other banks. However, deposit insurance removes the incentive for depositors to closely monitor lending and investing activities of their financial institutions, adding to the cost of the financial system. To reduce this distorting effect, some have proposed lowering the effective ceiling on insured deposits held by individuals and their families. But community bankers and their supporters argue that this would unfairly penalize small banks. Because of concern about possibly jarring the Nation's economy, regulators tend to repay both the insured and uninsured portions of deposits at large failed banks, but not at small banks. If insured deposits are reduced and people expect regulators to continue to protect large banks, depositors might switch from small rural banks to offices of large urban banks, making it difficult for rural banks to compete.

Agenda. Comprehensive banking legislation was proposed in the last session of Congress, but a coalition representing groups such as community banks, insurance agents, and retired people was able to delete those sections addressing interstate banking and additional bank powers.

Information Sources. Two U.S. Dept. of Agriculture, Economic Research Service, reports: J. M. McGlone, "Rural Businesses Voice Few Complaints About Their Bankers," *Rural Development Perspectives*, Vol. 7, Issue 2. D. L. Milkove and P. J. Sullivan, *Deregulation and the Structure of Rural Financial Markets*, RDRR-75, Feb. 1990.

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Issues for the 1990's: Rural Economy

Preferential Tax Treatment for Capital Gains

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Ron Durst (202) 219-0897

Issue. A major challenge facing the U.S. economy is the need to encourage greater investment to maintain a competitive edge in an increasingly interdependent world economy. Reinstating some form of preferential treatment of capital gains is one policy option being considered to encourage the formation of new businesses and increase investment. Preferential tax treatment of capital assets increases the relative rate of return on such assets by reducing potential income tax liability and provides incentives to invest in small business. Given the importance of capital income to farmers, the treatment of such income has important implications for farm output and asset values.

Context. The Federal income tax code has historically contained some form of preferential treatment for gains generated from capital assets. The preferential treatment of capital gains increases the rate of return to savings, and lowers the cost of capital, leading to an increase in the level of investment. That, in turn, raises gross national product (GNP). Since assets used in a trade or business are eligible for capital gains treatment, policies aimed at restoring some form of preferential treatment for capital assets have important implications for farmers. Agricultural assets eligible for treatment as capital income include breeding and dairy livestock and farmland. As a result of this treatment, capital gains is an important component of income for farmers. From 1987 to 1989, a minimum of 35 percent of farm sole proprietors reported capital gains. This compares to 11-13 percent of nonfarm returns over the same period. The average capital gain reported by farm sole proprietors ranged from slightly over \$13,000 to nearly \$16,000 from 1987 to 1989.

Between 1922 and 1986, as much as 60 percent of the gains from the sale of long-term capital assets were excluded from Federal income taxes. The Tax Reform Act of 1986 repealed the 60-percent exclusion for long-term gains and capped the maximum tax rate on realized capital gains at 28 percent, providing individuals subject to the maximum statutory marginal income tax rate a 3-percentage-point differential in tax rates. The repeal of the 60-percent exclusion for long-term capital gains resulted in a substantial increase in Federal income tax liabilities for farmers, especially livestock farmers. Repeal of the capital gains exclusion accounted for about half of the tax increase under the act, research estimates show. The resulting increase in tax liability associated with the sale of farmland that has been held for many years is a significant concern for farmers planning to dispose of farmland for retirement purposes. On the positive side, the repeal of the exclusion reduced the incentive to convert fragile rangeland and wetlands to cropland. Capital gains treatment was considered a major factor in such conversions.

At Stake. A lower tax rate on capital gains would reduce Federal income tax liability for many farmers. However, for both nonfarm returns and farm sole proprietors, a large portion of the resulting tax reductions would accrue to relatively high-income individuals. In 1989, approximately 48 percent of the capital gains reported by farm sole proprietors was reported by those with adjusted gross incomes above \$200,000.

Given other tax preferences in agriculture, a lower rate would encourage farm proprietors to adopt management practices designed to maximize income eligible for capital gains treatment. This lower rate would also spur investment in agricultural capital assets by nonfarm individuals. A lower tax rate on capital gains, if applicable to assets used in farming, would increase agricultural output and land values. The resulting increase in investment in agriculture would occur in a capital-intensive industry already characterized by excess capacity. The increased rate of return on farmland would be capitalized in land values, increasing current farmland prices.

Alternatives. Several alternatives relating to preferential tax treatment exist:

(1) Maintain the current 28-percent maximum tax rate on realized capital gains. Under current law, only individuals subject to the maximum 31-percent tax rate benefit from this differential treatment. These benefits would increase substantially if the top marginal income tax rate were increased to 36 percent. The 8-percentage-point differential could encourage individuals to invest more in agricultural assets such as farmland and breeding and dairy livestock to generate capital income rather than ordinary income.

(2) Index capital assets for inflation. Under current law, taxes are imposed on nominal changes in asset values. Indexation would ensure that only real gains, not inflationary gains, would be subject to taxation. The primary benefits of indexing in agriculture would accrue to owners of farmland held for a long time, since a large part of the increase in value is often attributed to inflation. Other farm assets eligible for capital gains treatment, such as livestock, generally have a zero basis and, hence, would not benefit from indexation.

(3) Enact legislation that provides a graduated exclusion depending upon the length of time the asset is held. For example, one recent proposal was to exclude the gains from assets held between 1 and 2 years, 2 and 3 years, and assets held 3 or more years at 10, 20, and 30 percent, respectively. This approach encourages long-term investment by increasing the tax benefits along with the length of time the asset is held. Since the exclusion of capital gains from taxable income is general, all farmers reporting capital gains would benefit, with the extent of benefits depending upon how long the assets were held and the individual's tax rate.

(4) Target preferential treatment to certain types of capital investments. A recent example is a proposal that would have excluded 50 percent of the capital gains from newly issued stock of small companies held for 5 or more years. The advantages of this type of policy are that it would target specific types of investment deemed to be the most effective in stimulating the economy and creating jobs. Forgone tax revenue would also be reduced relative to a general capital gains exclusion. The implications for agriculture would depend upon the type of investments targeted to receive preferential treatment. Agriculture would not be a major beneficiary of a capital gains exclusion restricted to newly issued stock in small companies.

Agenda. Since the Tax Reform Act of 1986 repealed the exclusion of 60 percent of capital gains from taxable income, various proposals have been made to reinstate some form of preferential treatment for capital gains. While the preferential treatment of capital gains is a policy option to stimulate investment in small business in order to generate jobs and increase economic growth, the extent of preferential treatment must be balanced with the constraints imposed by the Federal budget deficit.

Information Source. *Effects of Lower Capital Gains Taxes on Economic Growth*, Congressional Budget Office, Aug. 1990.

United States
Department of
Agriculture

Economic
Research
Service

Agriculture
Information
Bulletin
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Issues for the 1990's: Rural Economy

Rural Economic Disadvantage

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Issue. Several economic indicators suggest that rural conditions worsened during the 1980's. The rural unemployment rate rose rapidly during the 1980-82 recessions and had not fallen back to its 1979 level by the onset of the 1990-91 recession. Rural per capita income and earnings per job fell further behind urban income and earnings during the decade. The rural poverty rate increased. And, half of all rural counties lost population. These indicators appear to be symptoms of a growing rural disadvantage in the emerging national and global marketplaces, thereby raising questions about the future well-being of much of rural America.

Context. Entering the 1980's, rural America seemed poised for strong economic performance. Growth in population, employment, and income in the 1970's had exceeded that of urban areas, narrowing the historical lag in rural well-being and greatly reducing rural population loss. But, a combination of factors prevented rural areas from further narrowing the gap in the 1980's. The 1980-82 recessions hit rural areas much harder than urban areas, primarily because job losses were concentrated in production occupations in manufacturing firms, where a higher proportion of rural than urban employment is concentrated. Rural manufacturing employment recovered slowly, not surpassing the prerecession (1979) number of jobs until 1989. These problems in manufacturing were combined with a farm crisis in the mid-1980's and job losses in mining in the last half of the decade. Evidence suggests these cyclical changes were accompanied by a long-term shift in rural competitiveness. Structural change in goods production reflects increasing global competition, technological change continues to displace production workers, and growing specialized producer services bypass rural areas.

At Stake. Continued rural economic deterioration could lead to increased outmigration to urban areas. From 1986 to 1988, 192 rural counties experienced net outmigration and more deaths than births. Some small communities in these areas may discontinue services when the cost of providing them rises above the remaining residents' ability to pay. Outmigration is also a concern for rural areas because the young, highly educated comprise a disproportionate share of those who leave. If rural areas cannot find ways to attract or create jobs requiring the skills of highly educated people, they may lose the group most likely to be the catalyst for improving local conditions. The Nation may also lose from rural outmigration as the costs of providing services in increasingly congested cities rise.

Alternatives. Views on equity and economic efficiency condition responses to rural-urban inequality and rural economic problems. Tight State and Federal budgets severely limit what could be spent to relieve rural problems. And, the wide variety of rural conditions calls for an array of responses, not a simple one-program-fits-all approach.

The National Initiative on Rural America, begun in 1989, established the President's Council on Rural America, a group of 19 rural leaders from the public and private sectors, to provide guidance to the President in setting a national rural development policy agenda. It also initiated State Rural Development Councils to assess local rural development needs and coordinate delivery of Federal, State, local, and private programs that respond to those needs. Most States are in the process of setting up Councils (47 States and territories are expected to have Councils by the end of 1993).

Funding for rural development-related projects comes from numerous Federal, State, and local programs. For example, the Small Cities Urban Development Block Grant program is administered by the U.S. Department of Housing and Urban Development. Rural housing, electrification, and community facilities loan and grant programs are administered by various agencies in the U.S. Department of Agriculture (USDA). And, many States provide seed money to rural revolving business loan funds to which local governments often add their own contributions.

Agenda. The current Federal rural development agenda is built on the principle that local residents are the best judges of which rural development strategies are appropriate for their communities. Efforts to reduce the rural economic disadvantage in an era of tight government budgets will require creative input from all levels of government.

Information Source. U.S. Dept. of Agriculture, Economic Research Service, *Rural Conditions and Trends*, various issues.

Nonmetro economic indicators, 1979-91

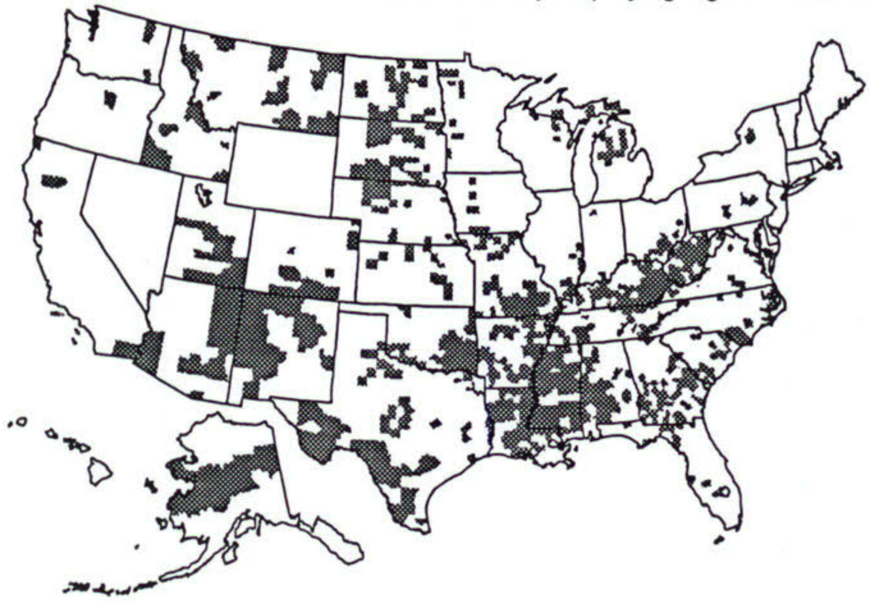
Unemployment, income, and earnings gaps widened during the 1980's, signaling increasing nonmetro disadvantage.

Year	Unemployment rate	Difference from metro unemp. rate	Real per capita income	Ratio to metro income	Real earnings per wage and salary job	Ratio to metro earnings
	Percent	*Percentage points*	*1990 dollars*	*Percent*	*1990 dollars*	*Percent*
1979	6.1	0.5	13,086	77.2	18,732	79.3
1980	8.0	1.1	12,768	75.4	18,489	79.0
1981	8.5	1.2	13,015	75.9	18,614	79.4
1982	11.1	1.8	12,786	74.9	18,614	78.6
1983	11.2	2.1	12,711	73.9	18,435	77.7
1984	9.1	2.1	13,318	74.3	18,522	77.4
1985	9.1	2.5	13,445	73.4	18,435	76.5
1986	9.0	2.6	13,715	73.5	18,394	75.5
1987	7.9	2.1	13,821	72.9	18,272	74.6
1988	6.9	1.8	14,117	72.3	18,189	73.5
1989	6.4	1.5	14,491	72.9	17,938	73.4
1990	6.5	1.3	14,600	73.4	17,791	73.1
1991	7.6	1.1	NA	NA	NA	NA

NA=Not available.

Nonmetro counties with more than one economic stress indicator

Most States have at least one nonmetro county displaying signs of economic stress.



Nonmetro counties with at least 2 of the following characteristics:

- in lowest 20 percent of all counties by 1990 per capita income.
- in lowest 20 percent of all counties by 1990 earnings per wage and salary job.
- in highest 20 percent of all counties by 1991 unemployment rate.
- in highest 20 percent of all counties by 1989 poverty rate.
- experienced both net out-migration and more deaths than births during 1986-88.

United States
Department of
Agriculture

Economic
Research
Service

Agriculture
Information
Bulletin
Number 664-15

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Issues for the 1990's: *Rural Economy*

Effects of the Investment Tax Credit on Farmers

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Issue. Continued slow growth of the U.S. economy has prompted policymakers to explore a variety of alternatives for stimulating job growth. One alternative that promotes capital formation, and thus more jobs, is an investment tax credit for purchases of machinery, equipment, and similar eligible property. Agriculture is a capital-intensive industry. Thus, restoration of the investment tax credit could offer important benefits to some farmers.

Context. Investment in depreciable capital has been eligible for a 7- or 10-percent investment tax credit at various times over the past 30 years. Eligible assets in farming have included farm machinery and equipment, as well as certain livestock and farm structures. The investment tax credit provides a substantial reduction in the cost of capital, encouraging investment in eligible assets. Research examining the effect of tax policies on investment in agricultural equipment during 1956-78 found that over 20 percent of net investment was attributed to tax policies. The investment tax credit was the most effective policy tool in stimulating investment, the research concluded. Repeal of the investment tax credit by the Tax Reform Act of 1986 resulted in a substantial increase in the cost of capital. The act reduced the stock of farm machinery and equipment by nearly $4 billion or nearly 25 percent relative to prior law, with the repeal of the investment tax credit accounting for approximately 89 percent of the decline, according to research examining the repeal's implications for capital investment.

While the investment tax credit is effective for stimulating investment, it favors certain forms of economic activity over others, discriminates among firms within a single industry, and encourages tax-motivated behavior. The tax credit distorts investment decisions by encouraging investments in assets or activities eligible for the credit rather than in those that would produce a greater economic return in its absence. In farming, the tax credit encouraged expanded investment despite excess supply for various farm commodities.

At Stake. The possibility that an investment tax credit in some form will be restored revives the debate regarding its implications for agriculture. The credit substantially reduces Federal income tax liability for many farmers. For example, prior to the repeal of the credit, about half of all farmers were eligible for an average tax credit of approximately $1,400 per year. The benefit to large farms was even greater, with nearly 85 percent of farms with gross receipts over $250,000 eligible for the investment tax credit. The average tax credit for these farms was over $10,000. The tax credit also lowers the cost of capital, which encourages investment in eligible assets. This increased investment benefits farm machinery dealers and other input suppliers. It also expands the production capacity of the sector and induces productivity growth. This results in expanded production, which results in lower prices, and increased government costs for some farm programs. For some farmers, the reduced farm income associated with lower prices could more than offset the benefit from the investment tax credit.

Alternatives. Policy alternatives include: (1) continue current policy (no investment tax credit), (2) restore a broad-based, 10-percent investment tax credit similar to that which existed prior to the Tax Reform Act of 1986, (3) provide an incremental tax credit that would be applicable only for investment above a specified base or threshold amount, or (4) enact a targeted investment tax credit that would be available only for investment in specified classes of property determined to be the most productive.

Choices among these alternatives will be influenced by the perceived need to stimulate the economy, the estimated cost of each of the alternatives, and the ability to identify acceptable revenue sources to offset the estimated tax losses.

Restoration of an across-the-board investment tax credit of 10 percent is the least likely due to the substantial revenue loss to the government. In farming alone, the government could lose as much as $1.5 billion a year in revenue. If a broad-based investment tax credit were enacted, it would likely be at a lower rate, reducing the effectiveness of the credit.

Enactment of an incremental tax credit for investment above a certain base would substantially reduce the tax drain. While this approach would favor some new businesses, it would provide little or no benefit to those firms that have invested heavily during the base period.

Under a targeted tax credit, a much narrower class of property would be eligible for a tax credit than prior to the 1986 law. While a targeted investment tax credit may be the most cost-effective alternative, it may be the most difficult to enact due to equity concerns that would arise by favoring certain industries or classes of assets over others. Under this alternative, the tax credit could be withheld on certain types of farm property, such as single-purpose agricultural structures, or on farms likely to expand production and increase the cost of government farm commodity programs in response to a tax credit.

Agenda. Numerous legislative proposals have been made to restore the investment tax credit. However, they have failed to gain broad-based support due to the rather large revenue loss associated with the proposed legislation. Nevertheless, given the recent support expressed for the enactment of an investment tax credit, a specific legislative initiative will likely be introduced early in 1993 as part of a fiscal stimulus package.

Information Sources. Michael LeBlanc, James Hrubovcak, Ron Durst, and Roger Conway, "Farm Machinery Investment and the Tax Reform Act of 1986," *Journal of Agricultural and Resource Economics*, Vol. 17, No. 1, Jul. 1992, pp. 66-79.

United States
Department of
Agriculture

Economic
Research
Service

Agriculture
Information
Bulletin
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Issues for the 1990's: Rural Economy

Improving Living and Working Conditions of Hired Farmworkers

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Issue. Hired farmworkers experience low wages, seasonal employment, weak attachment to the labor force, and limited options for higher paying jobs. In addition, many are excluded from coverage under basic worker protection programs generally available to other U.S. workers. Federal assistance programs targeted specifically to hired farmworkers frequently serve only a small portion of those eligible. These continuing disadvantages raise questions about the direction of efforts to improve their living and working conditions.

Context. Hired farmworkers comprise a small proportion of all U.S. wage and salary workers. But, they are an essential input to U.S. agriculture and contribute necessary labor during critical production periods. Almost half of all U.S. farms used hired labor in 1987; these farms produced about 84 percent of the total value of sales for farm products. Farmers spent almost $13 billion for labor in 1987, accounting for 12 percent of total farm production expenses. Labor costs on the more labor-intensive fruit, vegetable, and horticultural specialty farms accounted for 37-44 percent of total farm production expenses.

An average of 884,000 hired farmworkers were employed per week on U.S. farms in 1991, according to the latest data from the Current Population Survey. Hired farmworkers were more likely than all wage and salary employees to be young, male, and Hispanic and they had lower education levels. About 55 percent of hired farmworkers in 1991 had not completed high school, compared with 15 percent of all wage and salary workers. The median weekly earnings of full-time hired farmworkers was $240, or only 56 percent of the $427 received by all full-time wage and salary workers. Because of the seasonal nature of agriculture, many hired farmworkers are employed for only part of the year, but depend heavily on their farm earnings. Some hired farmworkers seek nonfarm work to supplement their incomes, but are often unable to compete for higher wage nonfarm jobs because of limited education and labor market skills.

Many Federal and State worker protection programs have special exemptions for agricultural employers based on employee numbers, days worked, or payroll size. These special exemptions for agriculture were applied largely because of perceived administrative and enforcement difficulties, concern over high labor costs for small farmers, and less representation of agricultural worker interests. Employees working on these exempt farms do not receive program benefits. The Fair Labor Standards Act, for example, requires only those employers using more than 500 man-days of agricultural labor during any calendar quarter of the preceding calendar year to pay the Federal minimum wage. Other Federal programs, including unemployment insurance, Social Security, and provisions of the Occupational Safety and Health Act (OSHA), also exempt some agricultural employers based on number of employees and/or size of payroll. Farmworkers are fully covered by State workers' compensation laws in only 14 States and partially covered in 23 others.

Federal programs sponsored by the U.S. Departments of Education, Labor, and Health and Human Services, among others, have provided a variety of employment, training, education, and health care services to hired farmworkers. Program evaluations suggest, however, that only a relatively small proportion of those eligible actually receive program assistance.

At Stake. Improvements in Federal assistance programs and basic workplace protection could help improve living and working conditions of many hired farmworkers. At the same time, these efforts could lead to greater Federal program costs and/or substantially higher labor costs to some farmers, particularly growers of fruit, vegetable, and horticultural crops. Increased labor costs could be passed on to consumers in the form of higher prices and could lead to increased foreign competition for some commodities.

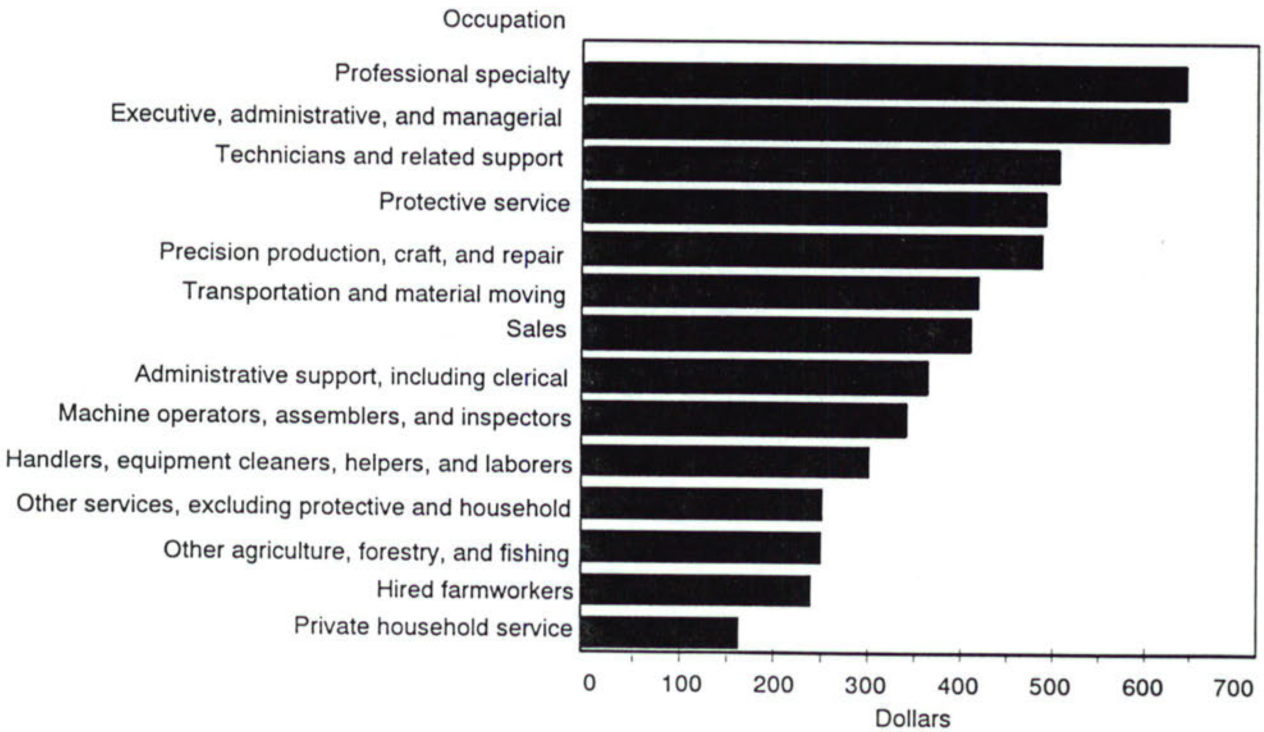
Alternatives. Two broad strategies could be followed. One strategy focuses on Federal assistance directed specifically to those low-skilled, low-income workers who depend heavily on farmwork. Current Federal programs provide a variety of employment, training, education, and health care services to hired farmworkers. Increased funding, expanded eligibility criteria, better service delivery, and improved coordination among programs could help extend program benefits, but at increased government costs. A second strategy calls for the removal or modification of agricultural exemptions in basic workplace protection programs. Such a strategy would extend to hired farmworkers the programs and benefits available to most other U.S. workers. Costs for expanding worker protection programs, such as minimum wage guarantees, unemployment insurance, occupational safety and health programs, and workers' compensation, would largely fall on farm employers currently exempt from program coverage. Costs of expanding Social Security coverage would be shared by both farm employers and their employees.

Agenda. Congressional hearings in 1990, 1991, and 1992 focused on a wide range of farm labor topics, including the socioeconomic well-being of hired farmworkers and the lack of workplace safeguards for many farm laborers. Although no legislative action is pending in early 1993, issues relating to the living and working conditions of hired farmworkers will likely receive continued congressional and media attention.

Information Sources. Two U.S. Dept. of Agriculture, Economic Research Service, reports: Victor J. Oliveira, *A Profile of Hired Farmworkers, 1990 Annual Averages*, AER-658, Feb. 1992 and Jack L. Runyan, *A Summary of Federal Laws and Regulations Affecting Agricultural Employers, 1992*, AIB-652, Aug. 1992. Also see: U.S. General Accounting Office, *Hired Farmworkers: Health and Well-Being at Risk*, report to congressional requesters, GAO/HRD-92-46, Feb. 1992.

Median weekly earnings of full-time wage and salary workers

Only private household service workers earned less than hired farmworkers.



Source: 1991 Current Population Survey microdata earnings file.

United States
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Economic
Research
Service

Agriculture
Information
Bulletin
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Issues for the 1990's: Rural Economy

Ethanol Production and the Rural Economy

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Issue. Among strategies to enhance farm income and provide rural jobs is development of new uses for farm products. The recent history of ethanol production illustrates how such strategies may unfold.

Context. U.S. ethanol production capacity is about 1.1 billion gallons a year at 39 currently operating facilities. Actual production was just over 900 million gallons in 1991. The eight largest plants account for 87 percent of total ethanol output and have production capacity ranging from 40 million to 280 million gallons per year. Large-scale ethanol plants are capital intensive, employing about three workers per million gallons of production. The larger plants use corn as a feedstock; seven of the eight largest plants are located in the Corn Belt. Nearly 96 percent of the Nation's ethanol is made from corn. About 6 percent of the 1990 corn crop was processed for ethanol.

More than half of ethanol plants produce less than 10 million gallons per year. Many of these are niche plants designed to use locally available, but commercially unusable, feedstocks. For example, cheese whey, potato waste, molasses, and brewery waste are relatively low-value food processing residues that can be transformed into a higher value product; their use solves a waste disposal problem. Such feedstocks often come at low or even negative cost to the ethanol producer. Use of an otherwise waste product as an input into the ethanol production process also provides benefits to society.

Demand for ethanol may grow rapidly due to clean air standards that are to be implemented in stages beginning in 1993. Substantial increases in ethanol production will result in crop substitution and increased farm and farm-related employment. Doubling ethanol production to 2 billion gallons per year by 1995 would require a 3.4-percent increase in production of corn, the primary feedstock for U.S. ethanol production. Prices and production of soybeans and other grains, such as wheat, sorghum, oats, and barley, would also be affected, some gaining and some losing value. Ethanol production will generally move the farm sector toward more market orientation as prices for corn and other grains move higher and as government deficiency payments decline.

Increasing annual ethanol production to 2 billion gallons by 1995 could create almost 28,000 jobs: 15,000 in farming and farm-related activities, 10,000 direct and indirect jobs from ethanol processing, and 3,000 temporary jobs from new plant construction. A majority of these jobs will be in the Midwest corn growing areas and many of the farm and farm-related jobs will go to rural residents. However, some farmers may choose to work additional hours rather than hire new workers and some of the new jobs may represent only part-time or seasonal employment opportunities. Nonfarm jobs associated with increasing the productive capacity of the ethanol industry, plant construction, and plant operation will be in communities that can meet the infrastructure and raw material needs of large plants. Industry experts suggest that an optimal-size, state-of-the-art ethanol facility should have a productive capacity of 100 million gallons per year.

At Stake. Hard-pressed rural communities are looking for ways to improve income and employment opportunities. A community's success in attracting a new 100-million-gallon ethanol facility will mean adding about 370 temporary jobs during the construction phase and about 840 permanent jobs during the operational phase. For communities with adequate resources, such increased employment means greater diversity in the economic base and more opportunities for growth.

Alternatives. Small- and medium-size cities in the Corn Belt are the most viable candidates to meet the basic requirements for large plants. The region produces abundant supplies of corn, its small- and medium-size cities have adequate labor to build and operate the plants, and many of the communities already have grain production, handling, processing, and transportation facilities as major parts of their economic base. Increased ethanol production will simply require an expansion of these sectors.

Most small, isolated rural communities cannot support large-scale ethanol plants. However, integrating ethanol production with other agricultural activities, such as production of a feedstock or use of byproducts, allows cost-competitive production on a smaller scale and offers additional employment opportunities. Examples of four integrated facilities are Garden City, Kansas, where ethanol byproducts are used in cattle feedlots and aquaculture, an Idaho plant where potato processing wastes are used as a feedstock, and two California plants where cheese whey from dairy processing is used as a feedstock.

Local communities may also benefit from emerging technologies that lower the cost of producing ethanol from renewable, nonfood feedstocks consisting primarily of cellulose. Organic wastes, agricultural crops, and forest products are all potential energy biomass feedstocks. Cellulosic conversion technology will make ethanol production possible in areas where sufficient biomass feedstock is available from agricultural activities (rural areas) or accumulated waste products (urban or suburban areas). Introducing energy crops (fast-growing trees and a variety of grasses) into the local agricultural economy, particularly on marginal lands, could lead to some increases in farm income and jobs, both on and off the farm.

Initially, biomass conversion plants are likely to be small-scale, perhaps 10 to 50 million gallons of ethanol per year. Some of these operations will locate in or near urban centers to solve problems of organic waste disposal. But, because most of the energy biomass will be grown in rural areas, the new biomass technology will improve the ability of rural America to effectively compete in ethanol production.

Agenda. The effect ethanol will have on farm income and rural job growth will largely be determined by the role it will play in meeting national clean air standards. Additional expansion of the industry will depend on a continuation of current favorable conditions, including extension of the Federal gasoline tax exemption. Ethanol's role will likely be debated for some time by public officials.

Information Sources. Two U.S. Dept. of Agriculture, Economic Research Service, reports: Neil Hohmann and C. Matthew Rendleman, *Emerging Technologies in Ethanol Production*, AIB-663, 1993, and Michael LeBlanc and John Reilly, *Ethanol: Economic and Policy Tradeoffs*, AER-585, 1988.

Jobs and ethanol

Almost 28,000 jobs could be added if annual ethanol production reaches 2 billion gallons.

Item	U.S. ethanol production capacity[1]	Employment gains: Construction[2]	Ethanol plant operation: Direct[3]	Ethanol plant operation: Indirect[4]	Ethanol plant operation: Total	Agriculture[5]	All
	Mil. gallons	*Jobs*					
Current production	920	--	--	--	--	--	--
Future production:							
Excess operating plant capacity	210	--	630	1,130	1,760	2,820	4,580
Proposed operating plant expansion	385	1,430	1,160	2,090	3,250	5,180	9,860
Proposed new plants	360	1,340	1,080	1,940	3,020	4,840	9,200
Idled plant capacity	183	--	550	990	1,540	2,460	4,000
Total	2,058	2,770	3,420	6,150	9,570	15,300	27,640

--=Not applicable. [1]Based on data from Information Resources, Inc. [2]A 100-million-gallon ethanol production facility takes 2 years and requires about 300 full-time construction workers. [3]Assumes that the labor requirement does not change as the industry expands. [4]Includes employment increases induced by increased consumer expenditures for goods and services. [5]Includes farm-related employment gains due to increased grain production. Total is allocated in proportion to all categories of future production.